



State Investment Commission

Monthly Meeting Minutes

Wednesday, October 26, 2011

9:00 a.m.

Room 135, State House

The Monthly Meeting of the State Investment Commission (SIC) was called to order at 9:00 a.m., Wednesday, October 26, 2011 in Room 135, State House.

I. Roll Call of Members

The following members were present: Ms. Rosemary Booth Gallogly, Mr. J. Michael Costello, Mr. Thomas Fay, Mr. Robert Giudici, Ms. Paula McNamara, Ms. Marcia Reback, Mr. Andrew Reilly and General Treasurer Gina Raimondo.

Also in attendance: Ms. Sally Dowling, of Adler Pollock, & Sheehan, and Mr. Joe Rodio Jr., of Rodio & Ursillo, Legal Counsel to the Commission; Mr. John Burns and Mr. Alan Emkin, of Pension Consulting Alliance (PCA), General Policy Consultant to the Commission; Mr. Thomas Lynch and Mr. Steve Nesbitt, of Cliffwater, Alternative Investment Consultant to the Commission; Mr. Nicholas Katsikis, of State Street Corporation; and members of the Treasurer's staff.

Treasurer Raimondo called the meeting to order at 9:10a.m.

II. Approval of Minutes

On a motion by Mr. Fay and seconded by Mr. Giudici, it was unanimously

VOTED: To approve the draft of the minutes of the September 28, 2011 meeting of the State Investment Commission.

III. PCA Presentation

Treasurer Raimondo asked PCA to do a portfolio review and risk update report. Mr. Emkin went over the 5 year and 10 year returns. Mr. Emkin stated interest rate risk is extremely risky. He explained a change in interest rate of 1% means ERSRI's bond portfolio will go down about 9% in market value on average. The risk of the equity markets is measured using the VIX index, which has doubled from recent lows. Mr. Emkin went on to explain the impact of the European debt crisis. He stated the real yield of holding bonds for 10 years is effectively zero, because of no inflation adjusted rate of return. Mr. Emkin reiterated this is an extremely challenging investment environment. He stated the Treasury currently returns 2.17% and most predict inflation to be 2.5% or 3% which limits purchasing power. The pension benefits, now linked to inflation will go up while the value of the bonds will shrink, which will make the plan worse without another source of capital.

Treasurer Raimondo agreed that while this is a difficult investment environment, all the decisions made this year were made to manage volatility and downside risk while sustaining return. The Treasurer asked Mr. Emkin if we should alter the plan and he said no, be patient; do not react to volatile daily events and stick to your plan.

Treasurer Raimondo informed the committee PCA, Cliffwater and the Treasurer's staff met a week ago to plan the next 5 or 6 months of meetings and ensure everyone is focused during this time of extreme volatility.

IV. Cliffwater Presentation

Mr. Nesbitt reviewed the recommendations of hedge fund allocations and sub-allocations. The objective of the hedge fund allocations is to earn returns consistent with or better than indices within those asset classes, but at a lower level of risk. Mr. Nesbitt recommended three funds in global equity: Samlyn Capital, Viking Global Equities and Mason Capital. Capula Global and Winton Futures were recommended in the absolute return bucket and Gracie Credit in the fixed income. Mr. Nesbitt gave an overview of each fund, explaining their history, giving an analysis of their operations and examining performance.

Ms. Booth Gallogly asked if there were regulatory actions against any of these funds and Mr. Nesbitt reaffirmed there were not. He explained they should expect returns at or above the global equity benchmark at half the risk.

Treasurer Raimondo urged the board to start thinking about risk like we think about returns.

Ms. Booth Gallogly inquired about exit penalties and Mr. Nesbitt explained the structure.

Mr. Costello asked about the different classes and Mr. Nesbitt recommended the share class most appropriate for each situation, sometimes the more liquid one or the less liquid, but with better terms.

On a motion by Mr. Reilly and seconded by Mr. Costello, it was unanimously

VOTED: to approve all funds on page two of the presentation, subject to negotiation and finalization of documentation after legal counsel review and after further diligence on asset classes.

V. Real Estate Portfolio Analysis

Mr. Lynch established the goal of real estate is to provide stable income in the portfolio. He explained implementation is key to accomplishing this goal. Mr. Lynch went on to say investments in core real estate will provide stable income, while private equity like real estate is more correlated with equity. He explained execution of time diversification is important in the process. ESRI has about \$100 million to achieve a 5% real estate allocation and can use this to accomplish its strategic goal.

Mr. Lynch said there is a large exposure to core strategies which assists with stability, but about half was to value added or opportunistic. The timing of these investments in 2006-2008 was unfortunate. After reviewing ERSRI's portfolio, Mr. Lynch says the majority are good managers and the challenge in manager quality is in the non-core space. Mr. Lynch thinks

there is good balance in the portfolio when looking at the property level and geographic location.

Mr. Costello stated they couldn't predict the real estate challenges, but asked if there was anything alarming the board should have known at the time. Mr. Lynch said they were good quality managers when hired. Mr. Costello mentioned the board stopped the real estate funding because the environment was so difficult.

Ms. Booth Gallogly asked about the lack of international exposure and Mr. Lynch explained the developed markets have been as challenging, but emerging markets have held steady.

The Treasurer established a real estate subcommittee comprised of Mr. Costello, Mr. Fay and Ms. McNamara.

VI. Corporate Governance

Treasurer Raimondo explained ERSRI doesn't have a corporate governance program regarding voting proxies. She explained ERSRI is behind our peers in this regard and since we are more indexed it is even more important to exercise shareholder rights and establish a plan.

Mr. Emkin explained the proxies votes are delegated to the index manager who votes on ERSRI's behalf, but with limited direction.

Treasurer Raimondo stated votes on executive compensation and executive performance might accomplish both. She proposed the question; do we really want to be involved with companies with human rights abuses, discrimination or risky environmental practices? She went on to explain that these practices add a level of risk.

Mr. Fay has a lot of experience in this area and offered some tentative plans to the board. A few board members reiterated corporate governance is an excellent idea and also their fiduciary responsibility.

VII. Meeting Schedule

On a motion from Ms. Reback and seconded by Ms. Giudici, it was unanimously **VOTED: To cancel the meeting scheduled for December 28, 2011.**

VIII. Legal Counsel Report

Ms. Dowling reported the paperwork from last meeting is on track for the finding in November. Many of the funds require certification that the board has authorized the General Treasurer to sign the paperwork and the prior resolution only dealt with private equity or real estate.

On a motion from Ms. Reback and seconded by Ms. Booth Gallogly, it was unanimously **VOTED: That the General Treasurer and the Chief Investment Officer, signing singly, hereby are, authorized, empowered and directed to execute subscription documents and limited liability company and limited partnership documents in connection with the Retirement fund's investment in hedge funds.**

IX. Chief Investment Officer Report

Mr. Goodreau mentioned there will soon be an enhanced report which incorporates with risk metrics. He pointed out; compared to our benchmark, we are 80 bps ahead of the year and 100 bps on the calendar year. On a relative basis the portfolio is doing better. Mr. Lynch pointed out risk is lower and returns are higher.

Mr. Izzo updated the board on the progress of the Ocean State Investment Pool. There were 8 respondents and they are conducting due diligence to narrow the field. They will make a recommendation and make presentations to the board next month.

Ms. Booth Gallogly offered the services of the division of municipal finances for communication efforts.

X. Treasurer's Report

Treasurer Raimondo recommended PCA do an RFI for rebalancing services.

XI. New Business

None this month

XII. Adjournment

There being no other business to come before the Board, on a motion by Ms. Gallogly and seconded by Mr. Reilly the meeting adjourned at 10:40 a.m.

Respectfully submitted,



Gina M. Raimondo
General Treasurer